

AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968, as amended. Filing is mandatory.

Local Government Type [x] City [] Township [] Village [] Other		Local Government Name City of Benton Harbor		County Berrien	
Audit Date 6/30/04		Opinion Date 12/17/04		Date Accountant Report Submitted to State: 3/8/05	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

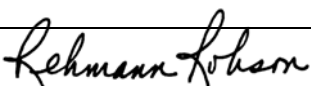
1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- | | | | | | |
|-------|-----|-------|----|----|--|
| [] | Yes | [x] | No | 1. | Certain component units/funds/agencies of the local unit are excluded from the financial statements. |
| [x] | Yes | [] | No | 2. | There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980). |
| [] | Yes | [x] | No | 3. | There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended). |
| [] | Yes | [x] | No | 4. | The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act. |
| [] | Yes | [x] | No | 5. | The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]). |
| [x] | Yes | [] | No | 6. | The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit. |
| [] | Yes | [x] | No | 7. | The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year). |
| [] | Yes | [x] | No | 8. | The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241). |
| [] | Yes | [x] | No | 9. | The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95). |

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	X		
Reports on individual federal financial assistance programs (program audits).			X
Single Audit Reports (ASLGU).	X		

Certified Public Accountant (Firm Name) REHMANN ROBSON GERALD J. DESLOOVER, CPA			
Street Address 5800 GRATIOT, PO BOX 2025		City SAGINAW	State MI
Accountant Signature 		Zip 48605	



CITY OF BENTON HARBOR, MICHIGAN

Financial Statements

**For The Year Ended
June 30, 2004**



REHMANN ROBSON

Certified Public Accountants

CITY OF BENTON HARBOR, MICHIGAN
For the Year Ended June 30, 2004

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REHMANN ROBSON

Certified Public Accountants

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INDEPENDENT AUDITORS' REPORT

December 17, 2004

Honorable Mayor and
Members of the City Commission
City of Benton Harbor, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the **City of Benton Harbor, Michigan**, as of and for the year ended June 30, 2004, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Benton Harbor's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Twin Cities Area Transportation Authority, the City's only discretely presented component unit. Those financial statements were audited by other auditors whose report was furnished to us, and our opinion, insofar as it relates to the amounts included for the Transportation Authority, is based solely on the report of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Benton Harbor, Michigan, as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparison for the general fund and enterprise zone special revenue fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 17, 2004, on our consideration of the City of Benton Harbor, Michigan's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants, in a separately issued single audit report. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis on pages 3-8 and the Pension System information on page 42 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Benton Harbor's basic financial statements. The combining fund financial statements and schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

A handwritten signature in black ink, reading "Lehmann Lohman". The signature is written in a cursive, flowing style with a large initial 'L'.

MANAGEMENT'S DISCUSSION and ANALYSIS

Management's Discussion and Analysis

The discussion and analysis of the City of Benton Harbor's financial performance provides an overview of the City's financial activities for the fiscal year ended June 30, 2004. Management has prepared the financial statements and the related footnote disclosures along with the discussion and analysis. Responsibility for the completeness and fairness of this information rests with the City's management.

About the City of Benton Harbor

The City is located in Berrien County in the southwestern corner of the lower peninsula of Michigan. The City is governed by an elected nine-member commission, but operates under a manager form of government.

Because of its economically distressed status, in 1986 Benton Harbor was designated as an Enterprise Zone City by the State under the Michigan Enterprise Zone Act of 1985, and is in fact the only city in the state to receive such a designation. This designation has allowed the City to redirect certain property tax collections as well as provide incentives for tax-base growth.

Under the Act, commercial/industrial businesses located within the City limits were given certain State tax benefits in return for real and personal property investments that increased taxable value. Organizations making this investment were then assessed property taxes at one-half the state-wide average millage rate (approximately 26 mills versus total local taxes of 60 mills) for 10 years. The entire tax levy (26 mills) for these "certified" properties became revenue to the City's General Fund. As the 10-year benefit period expires for these organizations, the General Fund tax revenue reverts back to the 18 operating mills approved by City voters.

The remaining commercial/industrial businesses in the City electing not to become "certified" continue to pay property taxes at voter-approved millage rates. However, the Enterprise Zone Act allows the City to recapture all local school district taxes. These taxes are reported as revenue in the Enterprise Zone Fund and restricted for capital/infrastructure expenditures to promote economic growth.

As "certified" businesses complete their 10-year certification period, General Fund revenue will decrease as indicated above. Enterprise Zone Fund revenue will increase due to the additional local school taxes recaptured on these properties.

The last commercial/industrial business certifications were approved in 1996 and the entire Enterprise Zone Act will sunset in the City's June 30, 2005 fiscal year.

Using this Annual Report

This annual report consists of a series of financial statements. The statement of net assets and the statement of activities provide information about the activities of the City as a whole and present a longer-term view of the City's finances. This longer-term view uses the accrual basis of accounting so that it can measure the cost of providing services during the current year, and whether the taxpayers have funded the full cost of providing government services.

The Fund financial statements present a short-term view; they tell us how the taxpayers' resources were spent during the year, as well as how much is available for future spending. Fund financial statements also report the City's operations in more detail than the government-wide financial statements by providing information about the City's most significant funds. The fiduciary fund statements provide financial information about activities for which the City acts solely as a trustee or agent for the benefit of those outside of the government.

The City as a Whole

The following table shows, in a condensed format, the net assets as of the current date and compared to the prior year:

City of Benton Harbor's Net Assets

	Governmental Activities		Business-type Activities		Total	
	2004	2003	2004	2003	2004	2003
Assets						
Current and other assets	\$ 2,846,575	\$ 2,340,518	\$ 9,733,441	\$ 9,706,237	\$ 12,580,016	\$ 12,046,755
Capital assets, net	12,984,809	12,790,588	3,255,087	3,515,164	16,239,896	16,305,752
Total assets	15,831,384	15,131,106	12,988,528	13,221,401	28,819,912	28,352,507
Liabilities						
Long-term liabilities	1,257,135	1,207,088	747,431	920,129	2,004,566	2,127,217
Other liabilities	1,476,142	1,441,191	832,535	606,896	2,308,677	2,048,087
Total liabilities	2,733,277	2,648,279	1,579,966	1,527,025	4,313,243	4,175,304
Net assets						
Invested in capital assets, net of related debt	12,774,914	12,679,007	2,536,027	2,661,623	15,310,941	15,340,630
Restricted	2,446,001	1,619,342	-	326,485	2,446,001	1,945,827
Unrestricted	(2,122,808)	(1,815,522)	8,872,535	8,706,268	6,749,727	6,890,746
Total net assets	\$ 13,098,107	\$ 12,482,827	\$ 11,408,562	\$ 11,694,376	\$ 24,506,669	\$ 24,177,203

The City's combined net assets increased 1.4 percent from a year ago - increasing from \$24,177,203 to \$24,506,669. As we look at the governmental activities separately from the business-type activities, we can see that the net assets increased almost 5.0 percent from a year ago.

The deficit in unrestricted net assets of governmental activities - that which can be used to finance day-to-day operations - increased by approximately \$307,000 for the governmental activities.

The following table shows the changes in the net assets during the current year and as compared to the prior year:

City of Benton Harbor's Changes in Net Assets

	Governmental Activities		Business-type Activities		Total	
	2004	2003	2004	2003	2004	2003
Revenues						
Program revenues:						
Charges for services	\$ 1,030,753	\$ 800,569	\$ 3,841,195	\$ 4,006,590	\$ 4,871,948	\$ 4,807,159
Operating grants and contributions	2,117,561	1,438,333	-	-	2,117,561	1,438,333
Capital grants and contributions	93,101	760,526	305,098	306,427	398,199	1,066,953
General revenues:						
Property taxes	4,150,309	3,787,651	-	-	4,150,309	3,787,651
State shared revenues	2,273,633	2,332,711	-	-	2,273,633	2,332,711
Grants and contributions not restricted to specific programs	228,236	136,395	-	-	228,236	136,395
Unrestricted investment earnings	7,562	24,745	10,156	17,224	17,718	41,969
Gain on sale of capital assets	132,475	71,608	-	-	132,475	71,608
Total revenues	<u>10,033,630</u>	<u>9,352,538</u>	<u>4,156,449</u>	<u>4,330,241</u>	<u>14,190,079</u>	<u>13,682,779</u>
Expenses						
Legislative	93,115	93,692	-	-	93,115	93,692
General government	2,360,421	2,455,971	-	-	2,360,421	2,455,971
Public safety	3,461,988	3,428,827	-	-	3,461,988	3,428,827
Public works	1,344,931	1,204,340	-	-	1,344,931	1,204,340
Recreation and cultural	64,487	164,307	-	-	64,487	164,307
Community and economic development	1,460,687	1,234,968	-	-	1,460,687	1,234,968
Other governmental activities	656,426	964,373	-	-	656,426	964,373
Interest on long-term debt	9,331	98,507	-	-	9,331	98,507
Utility services	-	-	4,205,429	3,525,273	4,205,429	3,525,273
Cemetery	-	-	203,798	179,684	203,798	179,684
Total expenses	<u>9,451,386</u>	<u>9,644,985</u>	<u>4,409,227</u>	<u>3,704,957</u>	<u>13,860,613</u>	<u>13,349,942</u>
Change in net assets before transfers	582,244	(292,447)	(252,778)	625,284	329,466	332,837
Transfers	<u>33,036</u>	<u>446,100</u>	<u>(33,036)</u>	<u>(446,100)</u>	<u>-</u>	<u>-</u>
Change in net assets	615,280	153,653	(285,814)	179,184	329,466	332,837
Net assets, beginning of year, as restated	<u>12,482,827</u>	<u>12,329,174</u>	<u>11,694,376</u>	<u>11,515,192</u>	<u>24,177,203</u>	<u>23,844,366</u>
Net assets, end of year	<u>\$ 13,098,107</u>	<u>\$ 12,482,827</u>	<u>\$ 11,408,562</u>	<u>\$ 11,694,376</u>	<u>\$ 24,506,669</u>	<u>\$ 24,177,203</u>

Governmental Activities

The City's total governmental revenues increased by approximately \$681,000. The increase, which represents approximately 7.3 percent, was primarily due to increases in property taxes, grant revenue and charges for services.

Expenses decreased by about \$194,000 during the year. Decreases resulted from lower recreation spending and general miscellaneous costs.

Business-type Activities

The City's business-type activities consist of Utility Services as well as the Cemetery operations. The City provides water to residents as well as sewage treatment services from the Benton Harbor/St. Joseph Joint Wastewater Treatment System.

Total revenues decreased by \$174,000. This resulted from a small decrease in revenue collected from customers. In addition, expenses increased approximately \$704,000 as the result of increases in water and sewer operating costs as well as increases in salaries and healthcare expenses.

The City's Funds

Our analysis of the City's major funds begins on page 11, following the government-wide financial statements. The fund financial statements provide detail information about the most significant funds, not the City as a whole. The City Commission creates funds to help manage money for specific purposes as well as to show accountability for certain activities, such as special property tax millages. The City's major funds for 2004 include the General Fund, the Enterprise Zone Fund, the Federal Grants Fund and the Utility Services Fund.

The General Fund pays for most of the City's governmental services. Significant services include police and fire protection services, which incurred expenses of approximately \$3,300,000 in 2004.

The Enterprise Zone Fund pays for City-wide capital/infrastructure improvements from property tax revenue as required by the Michigan Enterprise Zone Act.

The Federal Grants Fund accounts for HUD block grant funding of community development projects. Additional economic development funding was provided in 2004 through Brownfield Economic Development (BEDI) grants totaling \$494,000.

General Fund Budgetary Highlights

The City did not amend their budget during the year.

The most significant revenue budget variance was caused by the delayed sale of some Jean Klock Park land because the transaction was contested in court. The City had budgeted proceeds of \$500,000, which did not occur. Other revenue shortfalls included an almost 85% (\$135,000) reduction in anticipated entrance fees from Jean Klock Park, a continued fall-off in rental registration/inspection fees (\$100,000) and less than anticipated rental income from the City's land leases and public facilities (\$150,000).

On the expenditure side, general administration costs were almost double budgeted amounts due to increases in general liability insurance premiums, legal judgments, professional fees and capital outlay expenditures. Police Department costs exceeded budget due to the availability of additional revenue sources that allowed the department to add officers. However, the revenue will not be realized until Fiscal 2005. Rubbish collection fees continue to increase and exceeded budget by approximately \$77,000. Many other departments were at or below budget, which caused total General Fund expenditures to exceed budget by only \$56,000.

Capital Asset and Debt Administration

At the end of 2004, the City had approximately \$38.6 million invested in a broad range of capital assets, including buildings, police and fire equipment, and water and sewer lines. This amount included additions of \$1,046,000 during the year. In addition, the City has invested significantly in roads within the City. Infrastructure projects completed in 2004 are included in the \$1,046,000 above. Retroactive infrastructure to 1980 will be reported prior to June 30, 2007.

The City incurred additional debt in fiscal 2004 for equipment totaling \$129,000.

In 2005, the City will make the final payment on all Michigan Emergency Loans. These loans, totaling \$2,440,000, were issued in 1981 through 1985 to bring some financial stability to the City. While the City still struggles financially, all loan payments were made timely. At June 30, 2005, the City will have retired two debt issues, freeing up approximately \$125,000 of governmental fund revenue available for other uses.

Economic Factors and Next Year's Budgets and Rates

As discussed earlier, the phase out of the Enterprise Zone Act through fiscal 2005 will have some impact on both General Fund and Enterprise Zone Fund tax revenue (decrease and increase, respectively). Starting in fiscal 2006, the Enterprise Zone Fund will no longer receive property taxes and activity in this fund will be limited to using existing fund balance at that time. The City will then be exploring alternate ways to fund capital/infrastructure improvements required for continued economic growth.

The economic position of the City is closely tied to that of the State. For fiscal year 2004, the State revenue sharing provided 36 percent of the City's General Fund revenues. The State continues to reduce statutory revenue sharing to all local units of government. The State's budget for its year beginning October 1, 2004 contained an agreement for the cities, villages and townships to maintain revenue sharing funding at prior year level. However, this is likely to change. The State funding problems are believed to be a multiple-year situation and future decreases are likely.

As property tax revenue and state revenue sharing decrease (or at a minimum remain flat), controlling General Fund expenditures becomes a significant challenge. The City was able to favorably resolve the court challenge mentioned above related to the sale of a parcel of Jean Klock Park, which will add \$500,000 of General Fund revenue in fiscal 2005. This parcel will be developed into 27 residential lots. As lots are sold the City is entitled to receive 75% of the sales price, which will range from \$100,000 to \$400,000 per lot. It is anticipated that lot sales will occur over the next two to three years. The City will incur approximately \$600,000 of up-front infrastructure costs related to this development, which may be paid from the Permanent Public Improvement or Enterprise Funds. As houses are built, this property will add significant dollars to the City's property tax base over the next five years. There are also two more residential developments currently in the planning stages which would add property tax base and therefore General Fund tax revenue.

In January 2004, the City experienced a significant change in Administration. The November 2003 elections brought a new mayor and four new commissioners to the elected body. A new City Manager was hired in November 2003. The top priority of this Commission and City Manager is developing a deficit reduction plan to bring all City Funds to a positive financial position within five years. This plan was submitted to the State for approval in early calendar 2005.

Contacting the City's Management

This financial report is intended to provide our citizens, taxpayers, customers, and investors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional information, we welcome you to contact the Finance Department.

BASIC FINANCIAL STATEMENTS

GOVERNMENT-WIDE FINANCIAL STATEMENTS

City of Benton Harbor, Michigan
Statement of Net Assets
June 30, 2004

	Primary Government			Component Unit
	Governmental Activities	Business-type Activities	Total	Transportation Authority
Assets				
Cash and cash equivalents	\$ 601,316	\$ 359,099	\$ 960,415	\$ 40,015
Investments	-	305,894	305,894	-
Receivables, net	1,411,576	1,179,802	2,591,378	85,435
Internal balances	791,086	(791,086)	-	-
Prepaid items and other assets	-	94,377	94,377	93,193
Investment in joint venture	42,597	8,585,355	8,627,952	-
Capital assets not being depreciated	3,362,749	6,736	3,369,485	62,700
Capital assets being depreciated, net	9,622,060	3,248,351	12,870,411	987,781
 Total assets	 15,831,384	 12,988,528	 28,819,912	 1,269,124
Liabilities				
Accounts payable and accrued expenses	1,476,142	832,535	2,308,677	57,089
Long-term liabilities:				
Due within one year	395,564	196,375	591,939	-
Due in more than one year	861,571	551,056	1,412,627	-
 Total liabilities	 2,733,277	 1,579,966	 4,313,243	 57,089
Net assets				
Invested in capital assets, net of related debt	12,774,914	2,536,027	15,310,941	1,050,481
Restricted for:				
Debt service	641,534	-	641,534	-
Other purposes	1,804,467	-	1,804,467	-
Unrestricted	(2,122,808)	8,872,535	6,749,727	161,554
 Total net assets	 \$ 13,098,107	 \$ 11,408,562	 \$ 24,506,669	 \$ 1,212,035

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Activities
For the Year Ended June 30, 2004

Functions/Programs	Expenses	Program Revenues		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary government				
Governmental activities:				
Legislative	\$ 93,115	\$ -	\$ -	\$ -
General government	2,360,421	262,600	-	-
Public safety	3,461,988	182,089	80,820	-
Public works	1,344,931	-	917,650	-
Recreation and cultural	64,487	-	-	-
Community and economic development	1,460,687	45,311	1,119,091	93,101
Other governmental activities	656,426	540,753	-	-
Interest on long-term debt	9,331	-	-	-
Total governmental activities	<u>9,451,386</u>	<u>1,030,753</u>	<u>2,117,561</u>	<u>93,101</u>
Business-type activities:				
Utility services	4,205,429	3,667,285	-	305,098
Cemetery	203,798	173,910	-	-
Total business-type activities	<u>4,409,227</u>	<u>3,841,195</u>	<u>-</u>	<u>305,098</u>
Total primary government	<u>\$ 13,860,613</u>	<u>\$ 4,871,948</u>	<u>\$ 2,117,561</u>	<u>\$ 398,199</u>
Component unit				
Twin Cities Area Transportation Authority	<u>\$ 1,668,817</u>	<u>\$ 205,420</u>	<u>\$ 1,126,328</u>	<u>\$ 20,597</u>

Changes in net assets

General revenues:
Property taxes
State shared revenues
Grants and contributions not restricted to specific programs
Unrestricted investment earnings
Gain on sale of capital assets
Transfers - internal activities
Total general revenues and transfers
Change in net assets
Net assets, beginning of year
Net assets, end of year

The accompanying notes are an integral part of these financial statements.

Net (Expense) Revenue and Changes in Net Assets			
Primary Government			Component Unit
Governmental Activities	Business-type Activities	Total	Transportation Authority
\$ (93,115)	\$ -	\$ (93,115)	\$ -
(2,097,821)	-	(2,097,821)	-
(3,199,079)	-	(3,199,079)	-
(427,281)	-	(427,281)	-
(64,487)	-	(64,487)	-
(203,184)	-	(203,184)	-
(115,673)	-	(115,673)	-
(9,331)	-	(9,331)	-
(6,209,971)	-	(6,209,971)	-
-	(233,046)	(233,046)	-
-	(29,888)	(29,888)	-
-	(262,934)	(262,934)	-
(6,209,971)	(262,934)	(6,472,905)	-
-	-	-	(316,472)
4,150,309	-	4,150,309	59,225
2,273,633	-	2,273,633	-
228,236	-	228,236	-
7,562	10,156	17,718	852
132,475	-	132,475	-
33,036	(33,036)	-	-
6,825,251	(22,880)	6,802,371	60,077
615,280	(285,814)	329,466	(256,395)
12,482,827	11,694,376	24,177,203	1,468,430
\$ 13,098,107	\$ 11,408,562	\$ 24,506,669	\$ 1,212,035

FUND FINANCIAL STATEMENTS

City of Benton Harbor, Michigan
Balance Sheet
Governmental Funds
June 30, 2004

	General	Enterprise Zone	Federal Grants	Nonmajor Funds	Totals
Assets					
Cash and cash equivalents	\$ 337,276	\$ 81,997	\$ 75,170	\$ 106,873	\$ 601,316
Accounts receivable	443,391	-	1,321	-	444,712
Notes receivable	90,927	404,690	-	-	495,617
Due from other governments	264,834	-	69,816	136,597	471,247
Due from other funds	1,033,740	1,066,835	-	863,526	2,964,101
Advances to other funds	581,389	764,116	-	542,391	1,887,896
<u>TOTAL ASSETS</u>	\$ 2,751,557	\$ 2,317,638	\$ 146,307	\$ 1,649,387	\$ 6,864,889
<u>LIABILITIES AND FUND BALANCES</u>					
Liabilities					
Accounts payable	\$ 421,390	\$ 140,619	\$ 3,912	\$ 14,186	\$ 580,107
Accrued liabilities	236,615	1,452	9,722	-	247,789
Due to other governments	630,870	-	-	11,834	642,704
Due to other funds	1,849,582	109,288	292,910	75,757	2,327,537
Advances from other funds	1,084,262	-	49,825	599,287	1,733,374
Deferred revenue	-	404,690	-	-	404,690
Total liabilities	4,222,719	656,049	356,369	701,064	5,936,201
Fund balances (deficit)					
Reserved for long-term receivables	110,927	-	-	-	110,927
Reserved for advances	581,389	764,116	-	542,391	1,887,896
Unreserved:					
Undesignated (deficit)	(2,163,478)	897,473	(210,062)	-	(1,476,067)
Undesignated, reported in nonmajor:					
Special revenue funds (deficit)	-	-	-	(343,248)	(343,248)
Debt service funds	-	-	-	641,534	641,534
Permanent fund	-	-	-	107,646	107,646
Total fund balances (deficit)	(1,471,162)	1,661,589	(210,062)	948,323	928,688
<u>TOTAL LIABILITIES AND FUND BALANCES</u>	\$ 2,751,557	\$ 2,317,638	\$ 146,307	\$ 1,649,387	\$ 6,864,889

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Reconciliation of Fund Balances on the Balance Sheet
for Governmental Funds to Net Assets
of Governmental Activities on the Statement of Net Assets
June 30, 2004

Fund balances - total governmental funds	\$ 928,688
Amounts reported for <i>governmental activities</i> in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources, and therefore not reported in the funds.	
Add: capital assets not being depreciated	3,362,749
Add: capital assets being depreciated	22,276,752
Subtract: accumulated depreciation	(12,654,692)
Because the focus of governmental funds is on short-term financing, some assets will not be available to pay for current-period expenditures. Those assets (such as certain receivables) are offset by deferred revenues in the governmental funds, and thus are not included in fund balance.	
Add: deferred notes receivable	404,690
The government's investment in its joint venture is not a financial resource, and therefore not reported in the funds.	
Add: investment in joint venture	42,597
Certain liabilities, such as bonds payable, are not due and payable in the current period, and therefore are not reported in the funds.	
Subtract: loans and leases payable	(961,181)
Subtract: compensated absences	(295,954)
Subtract: accrued interest on long-term liabilities	(5,542)
Net assets of governmental activities	<u>\$ 13,098,107</u>

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balance
Governmental Fund
For the Year Ended June 30, 2004

	General	Enterprise Zone	Federal Grants	Nonmajor Funds	Totals
Revenue					
Taxes	\$ 2,549,792	\$ 1,275,110	\$ -	\$ 525,407	\$ 4,350,309
Federal sources	47,634	-	1,086,159	-	1,133,793
State sources	2,306,819	4,000	-	917,650	3,228,469
Licenses and permits	162,929	-	-	-	162,929
Fines and forfeits	54,013	-	-	-	54,013
Charges for services	823,553	90,621	-	-	914,174
Contributions	-	122,033	-	-	122,033
Interest	6,263	-	-	486	6,749
Other revenue	347,323	813	-	860	348,996
Total revenue	6,298,326	1,492,577	1,086,159	1,444,403	10,321,465
Expenditures					
Current:					
Legislative	92,549	-	-	-	92,549
General government	2,490,681	-	-	-	2,490,681
Public safety	3,262,780	-	-	-	3,262,780
Public works	372,205	-	-	887,110	1,259,315
Recreation and cultural	127,405	-	-	-	127,405
Community and economic development	146,029	781,380	1,148,452	23,968	2,099,829
Other	656,426	-	-	-	656,426
Debt service:					
Principal	27,772	-	-	98,000	125,772
Interest	164	-	-	3,625	3,789
Total expenditures	7,176,011	781,380	1,148,452	1,012,703	10,118,546
Revenue over (under) expenditures	(877,685)	711,197	(62,293)	431,700	202,919
Other financing sources (uses)					
Proceeds from long-term debt	126,086	-	-	-	126,086
Sale of capital assets	132,475	-	-	-	132,475
Transfers in	33,036	-	-	219,736	252,772
Transfers (out)	-	-	-	(219,736)	(219,736)
Total other financing sources (uses)	291,597	-	-	-	291,597
Net change in fund balances	(586,088)	711,197	(62,293)	431,700	494,516
Fund balances (deficit), beginning of year	(885,074)	950,392	(147,769)	516,623	434,172
Fund balances (deficit), end of year	\$ (1,471,162)	\$ 1,661,589	\$ (210,062)	\$ 948,323	\$ 928,688

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Reconciliation of the Statement of Revenue, Expenditures
and Changes in Fund Balances
of Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2004

Net change in fund balances - total governmental funds	\$ 494,516
Amounts reported for <i>governmental activities</i> in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation	
Add: capital outlay	995,469
Subtract: depreciation expense	(801,248)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds, but rather are deferred to the following fiscal year.	
Subtract: collections on notes receivable	(45,310)
The government's investment in its joint venture is not a financial resource, and therefore not reported in the funds.	
Add: increase in value of investment in joint venture	27,442
Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long term-liabilities.	
Add: principal payments on long-term liabilities	125,772
Subtract: lease proceeds received	(126,086)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.	
Add: change in accrued interest on bonds	(5,542)
Subtract: increase in the accrual of compensated absences	(49,733)
Change in net assets of governmental activities	<u>\$ 615,280</u>

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund
For the Year Ended June 30, 2004

	Original/ Final Budget	Actual	Actual over (under) Final Budget
Revenue			
Taxes			
Real and personal property taxes	\$ 1,874,000	\$ 2,096,905	\$ 222,905
Delinquent taxes	210,000	200,305	(9,695)
Payments in lieu of taxes	400,000	200,000	(200,000)
Other taxes	48,000	52,582	4,582
Total taxes	2,532,000	2,549,792	17,792
Federal sources	-	47,634	47,634
State sources			
State shared revenue	2,505,000	2,273,633	(231,367)
State grants	10,000	33,186	23,186
Total state sources	2,515,000	2,306,819	(208,181)
Licenses and permits	52,500	162,929	110,429
Fines and forfeits	150,000	54,013	(95,987)
Charges for services			
Cable franchise fees	40,000	41,472	1,472
Rubbish fees	500,000	540,753	40,753
Registration fees	60,000	66,328	6,328
Administrative fees	175,000	175,000	-
Total charges for services	775,000	823,553	48,553
Interest	45,000	6,263	(38,737)
Other revenue			
Rental income	188,000	119,947	(68,053)
Reimbursements	86,500	187,408	100,908
Miscellaneous	263,100	39,968	(223,132)
Total interest and rentals	537,600	347,323	(190,277)
Total revenue	6,607,100	6,298,326	(308,774)

continued...

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund (Continued)
For the Year Ended June 30, 2004

	Original/ Final Budget	Actual	Actual over (under) Final Budget
Expenditures			
Legislative			
Mayor / Commission	\$ 127,050	\$ 92,549	\$ (34,501)
General government			
City Manager	202,597	121,135	(81,462)
City Assessor	221,724	153,194	(68,530)
City Attorney	170,000	122,295	(47,705)
City Clerk	171,122	141,922	(29,200)
Elections	28,980	18,204	(10,776)
Personnel department	119,976	100,345	(19,631)
Finance department	308,600	263,004	(45,596)
Purchasing / risk management	-	5,556	5,556
City hall and grounds	298,663	291,988	(6,675)
General administration	645,500	1,273,038	627,538
Total general government	2,167,162	2,490,681	323,519
Public safety			
Police	1,627,085	1,813,598	186,513
Police general employees	603,942	248,970	(354,972)
Fire	1,065,904	1,039,422	(26,482)
Inspection department	206,702	160,790	(45,912)
Total public safety	3,503,633	3,262,780	(240,853)
Public works			
City Engineer	-	79,341	79,341
Public works administration	162,947	89,302	(73,645)
Public works stabilization	5,300	937	(4,363)
Streets and lighting	231,500	202,625	(28,875)
Total public works	399,747	372,205	(27,542)
Recreation and cultural			
Parks department	-	56,252	56,252
Armory	25,000	57,003	32,003
Recreation	101,658	14,150	(87,508)
Total recreation and cultural	126,658	127,405	747

continued...

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund (Concluded)
For the Year Ended June 30, 2004

	Original/ Final Budget	Actual	Actual over (under) Final Budget
Expenditures (concluded)			
Community and economic development			
Economic development	\$ 100,627	\$ 146,029	\$ 45,402
Other expenditures			
Rubbish collection	500,000	577,084	77,084
Aid to other agencies	120,000	79,342	(40,658)
Total other expenditures	620,000	656,426	36,426
Debt service			
Principal	75,000	27,772	(47,228)
Interest	-	164	164
Total debt service	75,000	27,936	(47,064)
Total expenditures	7,119,877	7,176,011	56,134
Revenue over (under) expenditures	(512,777)	(877,685)	(364,908)
Other financing sources (uses)			
Loan proceeds	-	126,086	126,086
Sale of capital assets	600,000	132,475	(467,525)
Transfers in	-	33,036	33,036
Total other financing sources (uses)	600,000	291,597	(308,403)
Net change in fund balances	87,223	(586,088)	(673,311)
Fund balance (deficit), beginning of year	(885,074)	(885,074)	-
Fund balance (deficit), end of year	<u>\$ (797,851)</u>	<u>\$ (1,471,162)</u>	<u>\$ (673,311)</u>

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balance
Budget and Actual
Enterprise Zone
For the Year Ended June 30, 2004

	Original Budget	Final Budget	Actual	Actual over (under) Final Budget
Revenue				
Taxes	\$ 807,679	\$ 807,679	\$ 1,275,110	\$ 467,431
State sources	42,617	42,617	4,000	(38,617)
Charges for services	-	-	90,621	90,621
Contributions	-	-	122,033	122,033
Interest	-	-	813	813
Total revenue	850,296	850,296	1,492,577	642,281
Expenditures				
Community and economic development:				
City development	1,218,577	416,419	690,709	274,290
Administration	50,000	50,000	90,671	40,671
Total expenditures	1,268,577	466,419	781,380	314,961
Net changes in fund balances	(418,281)	383,877	711,197	327,320
Fund balances, beginning of year	950,392	950,392	950,392	-
Fund balances end of year	\$ 532,111	\$ 1,334,269	\$ 1,661,589	\$ 327,320

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Net Assets
Proprietary Funds
June 30, 2004

	Utility Services	Cemetery (Nonmajor)	Totals
Assets			
Current assets:			
Cash and cash equivalents	\$ 301,963	\$ 57,136	\$ 359,099
Accounts receivable	633,439	1,751	635,190
Due from other governments	544,612	-	544,612
Due from other funds	206,123	2,399	208,522
Inventory	-	69,145	69,145
Total current assets	1,686,137	130,431	1,816,568
Noncurrent assets:			
Restricted investments	-	305,894	305,894
Investment in joint venture	8,585,355	-	8,585,355
Bond issuance costs	25,232	-	25,232
Capital assets not being depreciated	6,626	110	6,736
Capital assets being depreciated, net	3,191,403	56,948	3,248,351
Total noncurrent assets	11,808,616	362,952	12,171,568
Total assets	13,494,753	493,383	13,988,136
Liabilities			
Current liabilities:			
Accounts payable	233,023	14,947	247,970
Accrued liabilities	98,556	-	98,556
Due to other governments	486,009	-	486,009
Due to other funds	810,328	34,758	845,086
Advances from other funds	-	154,522	154,522
Current portion of long-term debt	185,327	11,048	196,375
Total current liabilities	1,813,243	215,275	2,028,518
Long-term liabilities:			
Due in more than one year	514,847	36,209	551,056
Total liabilities	2,328,090	251,484	2,579,574
Net assets			
Invested in capital assets, net of related debt	2,509,841	26,186	2,536,027
Restricted	-	305,894	305,894
Unrestricted (deficit)	8,656,822	(90,181)	8,566,641
Total net assets	\$ 11,166,663	\$ 241,899	\$ 11,408,562

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Revenue, Expenses
and Changes in Fund Net Assets
Proprietary Funds
For the Year Ended June 30, 2004

	Utility Services	Cemetery (Nonmajor)	Totals
Operating revenue			
Charges for services:			
Water sales	\$ 2,503,573	\$ -	\$ 2,503,573
Sewer sales	1,039,671	-	1,039,671
Other	124,041	173,910	297,951
	<hr/>	<hr/>	<hr/>
Total operating revenue	3,667,285	173,910	3,841,195
	<hr/>	<hr/>	<hr/>
Operating expense			
Cost of services:			
Water	2,878,199	-	2,878,199
Sewer	622,575	-	622,575
Cemetery	-	174,772	174,772
Administrative costs	354,079	-	354,079
Depreciation	283,578	27,339	310,917
	<hr/>	<hr/>	<hr/>
Total operating expense	4,138,431	202,111	4,340,542
	<hr/>	<hr/>	<hr/>
Operating income (loss)	(471,146)	(28,201)	(499,347)
	<hr/>	<hr/>	<hr/>
Non-operating revenue (expenses)			
Interest income	452	9,704	10,156
Income from joint venture	305,098	-	305,098
Interest expense	(53,558)	(1,687)	(55,245)
Amortization of bond issuance costs	(13,440)	-	(13,440)
	<hr/>	<hr/>	<hr/>
Total non-operating revenue (expenses)	238,552	8,017	246,569
	<hr/>	<hr/>	<hr/>
Income (loss) before transfers	(232,594)	(20,184)	(252,778)
	<hr/>	<hr/>	<hr/>
Transfers in (out)			
Transfers (out)	(33,036)	-	(33,036)
	<hr/>	<hr/>	<hr/>
Change in net assets	(265,630)	(20,184)	(285,814)
	<hr/>	<hr/>	<hr/>
Net assets, beginning of year	11,432,293	262,083	11,694,376
	<hr/>	<hr/>	<hr/>
Net assets, end of year	<u>\$ 11,166,663</u>	<u>\$ 241,899</u>	<u>\$ 11,408,562</u>

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Cash Flows
Proprietary Funds
For the Year Ended June 30, 2004

	Utility Services	Cemetery (Nonmajor)	Totals
Cash flows from operating activities			
Cash received from customers	\$ 3,631,227	\$ 173,880	\$ 3,805,107
Cash payments to suppliers for goods and services	635,666	79,053	714,719
Cash payments to employees for services	(4,141,534)	(203,797)	(4,345,331)
Net cash provided by (used in) operating activities	125,359	49,136	174,495
Cash flows from non-capital financing activities			
Transfers (out)	(33,036)	-	(33,036)
Cash flows from capital and related financing activities			
Purchase of capital assets	(47,769)	(3,072)	(50,841)
Proceeds from capital lease	3,244	-	3,244
Interest payments	(53,558)	(1,687)	(55,245)
Principal payments	(160,056)	(10,815)	(170,871)
Net cash used in capital and related financing activities	(258,139)	(15,574)	(273,713)
Cash flows from investing activities			
Interest income	452	9,929	10,381
Net increase (decrease) in cash and cash equivalents	(165,364)	43,491	(121,873)
Cash and cash equivalents, beginning of year	467,327	13,645	480,972
Cash and cash equivalents, end of year	<u>\$ 301,963</u>	<u>\$ 57,136</u>	<u>\$ 359,099</u>

continued...

City of Benton Harbor, Michigan
Statement of Cash Flows
Proprietary Funds (Concluded)
For the Year Ended June 30, 2004

	Utility Services	Cemetery (Nonmajor)	Totals
Cash flows from operating activities			
Operating income (loss)	\$ (471,146)	\$ (28,201)	\$ (499,347)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:			
Depreciation	283,578	27,339	310,917
Changes in assets and liabilities:			
Accounts receivable	629,677	409	630,086
Due from other governments	(544,612)	-	(544,612)
Due from other funds	(121,123)	(439)	(121,562)
Inventory	-	338	338
Accounts payable	(274,536)	14,933	(259,603)
Accrued liabilities	(766)	-	(766)
Due to other governments	486,009	-	486,009
Due to other funds	150,207	34,758	184,965
Advances from other funds	-	(1)	(1)
Compensated absences	(11,929)	-	(11,929)
Net cash provided by operating activities	<u>\$ 125,359</u>	<u>\$ 49,136</u>	<u>\$ 174,495</u>

Non-cash transactions

There were no non-cash transactions during the fiscal year.

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Fiduciary Net Assets
Fiduciary Funds
June 30, 2004

	<u>Pension Trust Funds</u>
Assets	
Cash and cash equivalents	\$ 146,010
Investments:	
Corporate bonds	5,987,685
Corporate stocks	9,189,654
US Government securities	2,404
Money market	206,316
Receivables:	
Accrued interest	33,017
Other	<u>371,255</u>
 Total assets	 <u>15,936,341</u>
 Liabilities	
Due to resigned employees	25,227
Accrued and other liabilities	<u>189,956</u>
 Total liabilities	 <u>215,183</u>
 Net Assets	
Held in trust for pension benefits and other purposes	 <u><u>\$ 15,721,158</u></u>

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Changes in Fiduciary Net Assets
Fiduciary Funds
For the Year Ended June 30, 2004

	<u>Pension Trust Funds</u>
Additions	
Taxes	\$ 229,451
Contributions:	
Employer	181,603
Employee	189,829
Total contributions	<u>371,432</u>
Investment earnings:	
Net appreciation in fair value of investments	1,121,130
Interest and dividends	473,702
Net investment earnings	<u>1,594,832</u>
Total additions	<u>2,195,715</u>
Deductions	
Pension benefits paid directly to participants	1,157,655
Administrative expenses	<u>156,324</u>
Total deductions	<u>1,313,979</u>
Change in net assets	881,736
Net assets, beginning of year	<u>14,839,422</u>
Net assets, end of year	<u><u>\$ 15,721,158</u></u>

The accompanying notes are an integral part of these financial statements.

NOTES to the FINANCIAL STATEMENTS

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the City of Benton Harbor (the “City”) conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The following is a summary of the significant accounting policies used by the City of Benton Harbor.

Reporting Entity

The City of Benton Harbor is governed by an elected nine-member commission. The accompanying financial statements present the City and its component units, entities for which the City is considered to be financially accountable. Although blended component units are legal separate entities, in substance, they are part of the City’s operations. Each discretely presented component unit is reported in a separate column in the government-wide financial statements to emphasize that it is legally separate from the City (*see discussion below for description*).

Blended Component Unit – The City of Benton Harbor blends one component unit, the Economic Development Corporation (the “Corporation”). The Corporation was established to encourage the location and expansion of industrial/commercial enterprises with the City limits on the City’s behalf. The City provides all administrative functions of the Corporation and appoints two commission members to the Corporation’s nine-member board. The Economic Development Corporation has been blended with the City’s special revenue funds and is considered a non-major fund.

Discretely Presented Component Unit – The City discretely presents one component unit in these financial statements, the Twin Cities Area Transportation Authority (the “Authority”). The Authority was incorporated in the State of Michigan on July 1, 1974 under Public Act 55 of 1963. The purpose of the Authority is to acquire, own, operate, and manage a public transportation system within the boundaries of the City of Benton Harbor, its only participating municipality. Given that the City has significant influence over the Authority and is the only participating municipality, the Twin Cities Area Transportation Authority is a component unit of the City of Benton Harbor. The Twin Cities Area Transportation Authority uses enterprise fund accounting. A complete financial report can be obtained from the Twin Cities Area Transportation Authority at 275 East Wall Street, Benton Harbor, MI 49023-0837, Telephone (269) 927-2268.

Jointly Governed Organizations

Southwest Michigan Regional Airport Authority – In fiscal 1998, four municipalities approved the establishment of an Airport Authority to oversee airport operations. Operations are partially funded by property taxes. In late July 1998, control of airport operations was transferred to the Authority. The Authority is governed by a board of four members, including one from each participating municipality. On dissolution, net assets will be shared on a prorata basis based on amounts contributed to the Authority. The City’s equity share was 4.9 percent at June 30, 2004. Based on audited financial statements, an equity interest has been recorded in the City’s basic financial statements as a governmental activity.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Benton Harbor-St. Joseph Joint Sewage Disposal Plant – The City is a participant with the City of St. Joseph in a joint venture to provide sanitary sewage treatment and collection facilities for the residents of these communities. The Benton Harbor-St. Joseph Joint Wastewater Treatment Plant was created for that purpose. Upon dissolution of the Plant, the net assets will be shared on an equal basis with the City of St. Joseph. The Plant is governed by a board of eight members consisting of three members each from Benton Harbor and St. Joseph and two members chosen from neighboring communities. The City's net investment and its share of the operating results of the Plant are reported in the City's Utility Services Fund (a business type activity).

"Corridor" Corporation – The City of Benton Harbor formed a development corporation with Cornerstone Alliance, a nonprofit organization established to promote economic growth in Benton Harbor and surrounding communities. The intent of this organization is to promote economic development in the "Benton Harbor Airport Corridor". The entity is owned 50 percent by the City and 50 percent by Cornerstone. The City contributed City owned property to the corporation. Cornerstone Alliance has incurred expenses on behalf of this corporation totaling \$117,650. These amounts are reflected as accounts receivable on Cornerstone's records, repayment which is dependent on future development of property held by "Corridor" Corporation. The only significant activity in the "Corridor" Corporation to date is the contribution of the property. In the future, when development activity begins, this investment will be accounted for on the equity method.

Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include: (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment; and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenue.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, expenditures relating to compensated absences, and claims and judgments are recorded only when payment is due.

Property taxes, state-shared revenue, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenue of the current fiscal period. All other revenue items are considered to be available only when cash is received by the City.

The City reports the following major governmental funds:

The General Fund is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The Enterprise Zone Fund is a special revenue fund that accounts for property taxes provided by the Michigan Enterprise Zone Act that are restricted for capital/infrastructure improvements.

The Federal Grants Fund is a special revenue fund that accounts for the administration of programs financed by federal grants and contracts.

The City reports the following major proprietary fund:

The Utility Services Fund accounts for the activities of the City's water distribution and wastewater treatment systems.

Additionally, the City reports the following fund types:

Special revenue funds. These funds account for revenue sources that are legally restricted to expenditures for specific purposes not including capital projects or permanent funds.

Debt service funds. These funds account for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Permanent fund. This fund accounts for resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support specified government programs.

Pension trust funds. These funds account for the activities of both the General Employees and Police and Fire Employees' retirement systems, which accumulate resources for pension benefit payments to qualified employees.

Private sector standards of accounting issued prior to December 1, 1989 are generally followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with the standards of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City has elected not to follow subsequent private sector standards.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the City's water/sewer function and various other functions of the City. Eliminations of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as program revenue include: (1) charges to customers or applicants for goods, services, or privileges provided; (2) operating grants and contributions; and (3) capital grants and contributions. Internally dedicated resources are reported as general revenue rather than as program revenue. Likewise, general revenue includes all taxes.

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services in connection with a proprietary fund's principal ongoing operations. The principal operating revenue of our proprietary funds relates to charges to customers for sales and services. The Utility Services Fund also recognizes the portion of tap fees intended to recover current costs (e.g., labor and materials to hook up new customers) as operating revenue. Operating expenses for proprietary funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

Assets, Liabilities, and Net Assets or Equity

Bank Deposits and Investments – Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with a maturity of three months or less when acquired. Investments are stated at fair value.

Receivables and Payables – In general, outstanding balances between funds are reported as "due to/from other funds." Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as "advances to/from other funds." Any residual balances outstanding between the governmental activities and the business-type activities are reported in the government-wide financial statements as "internal balances."

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

All trade and property tax receivables are shown as net of allowance for uncollectible amounts. Property taxes are levied on each July 1 on the taxable valuation of property as of the preceding December 31. Taxes are considered delinquent on July 1 of the following year, at which time penalties and interest are assessed.

Inventories and Prepaid Items – Inventories are valued at cost, on a first-in, first-out basis. Certain payments to vendors reflect costs applicable to future fiscal years and are recorded as prepaid items in both government-wide and fund financial statements.

Capital Assets – Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the City as assets with an initial individual cost of more than \$1,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

Capital assets are depreciated using the straight-line method over the following useful lives:

Roads and sidewalks	10 to 15 years
Land improvements	5 to 75 years
Buildings and building improvements	10 to 30 years
Water and sewer distribution systems	12 to 75 years
Vehicles	5 years
Computer equipment	5 years
Office equipment	7 years
Office furnishings	7 years
Other tools and equipment	7 years

Infrastructure has only been recorded for projects that occurred subsequent to June 30, 2002. Retroactive infrastructure to 1980 will be reported prior to June 30, 2007.

Compensated Absences (Vacation and Sick Leave) – It is the City's policy to permit employees to accumulate earned but unused sick and vacation pay benefits. There is no liability for unpaid accumulated sick leave except for amounts accumulated by police and fire employees. Vacation pay for all employees and sick pay for police and fire employees is accrued when incurred in the government-wide and proprietary fund financial statements. A liability for these amounts is reported in governmental funds only for employee terminations as of year end.

Long-term Obligations – In the government-wide financial statements and the proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund-type statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt. In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs during the current period. The face amount of debt issued is reported as other

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

financing sources. Premiums received on debt issuances are reported as other financing sources while discounts are reported as other financing uses. Issuance costs are reported as debt service expenditures.

Fund Equity – In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose.

2. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary Information – Annual budgets are adopted on a basis consistent with generally accepted accounting principles for the General Fund and all Special Revenue Funds except the Federal and State Grant funds, which are budgeted on a project-length-basis. The annual budget is prepared by the City management and adopted by the City Commission; subsequent amendments are approved by the City Commission. All annual appropriations lapse at fiscal year end and encumbrances are not included as expenditures. During the year, the budget was amended in a legally permissible manner.

The budget document presents information by fund, function, department, and line items. The legal level of budgetary control adopted by the governing body is the department level. Expenditure budget overruns are as reported in the statement of revenue, expenditures, and changes in fund balance – budget and actual for the General Fund and Enterprise Zone Fund.

Fund Deficits – The City has accumulated unreserved fund deficits in the following individual funds:

<u>Fund</u>	<u>Balance</u>
General Fund	\$(2,163,478)
Special Revenue Funds:	
Major Streets Fund	(73,824)
Local Streets Fund	(203,403)
Federal Grants Fund	(210,062)
State Grants Fund	(66,021)
Enterprise Fund – Cemetery Fund	(90,181)

Deficit Plan

The City of Benton Harbor General Fund has a total deficit fund balance of \$1,471,162 for the year ended June 30, 2004 and is structuring a five-year plan to reduce this deficit. This deficit reduction was included in the City's budget beginning in fiscal year 2004, and will continue to be until the deficit is eliminated. Overall, the plan will seek to increase revenues and reduce costs while maintaining service levels. In addition, the City is looking at a reduction in normal expenditures by management controls and restructuring processes and procedures. The City hopes to achieve this through improved rubbish collections, land sales of beach-front property, sales of tax-reverted property, and property reassessments. The City looks to control expenditures through management/departmental oversight of cell phone usage and gasoline consumption, as well as other general costs.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

3. DEPOSITS AND INVESTMENTS

Michigan Compiled Laws, Section 129.91, authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The local unit is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United States banks; commercial paper rated within the two highest classifications, which mature not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions, which are rated as investment grade; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

The City deposits funds at various local banks. The investment policy adopted by the Board in accordance with Public Act 196 of 1997 has authorized investment in bonds and securities of the United States government and bank accounts and CDs. The City of Benton Harbor's deposits and investment policies are in accordance with statutory authority.

At year end, the deposits and investments were reported in the basic financial statements in the following categories:

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Fiduciary Funds</u>	<u>Total Primary Government</u>	<u>Component Units</u>
Cash and cash equivalents	\$ 601,316	\$ 359,099	\$ 146,010	\$ 1,106,425	\$ 40,015
Investments	-	305,894	15,386,059	15,691,953	-
Total	<u>\$ 601,316</u>	<u>\$ 664,993</u>	<u>\$ 15,532,069</u>	<u>\$ 16,798,378</u>	<u>\$ 40,015</u>

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

The breakdown between deposits and investments for the year ended June 30, 2004, is as follows:

	Primary Government	Component Units
Bank deposits (checking accounts, savings accounts, and certificates of deposit)	\$ 1,410,199	\$ 39,785
Investments in securities, mutual funds and similar vehicles	15,386,059	-
Petty Cash	2,120	230
Total	\$ 16,798,378	\$ 40,015

Primary Government - The bank balance of the City's deposits is \$1,552,408, of which \$438,689 is covered by federal depository insurance, and \$1,113,719 is uninsured.

Component Unit - The deposits of the component unit were reflected in the accounts of the bank at \$39,785, all of which was covered by federal depository insurance.

Investments are categorized into these three categories of credit risk:

Category 1 – Insured or registered, or securities held by the City of Benton Harbor or its agent in the City's name;

Category 2 – Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the City's name; and

Category 3 – Uninsured and unregistered, with securities held by the counterparty or by its trust department or agent but not in the City's name.

	Category			Reported Amount (Fair Value)
	1	2	3	
Primary Government				
Corporate Bonds	\$ -	\$ -	\$ 5,987,685	\$ 5,987,685
Common Stock	-	-	9,189,654	9,189,654
U.S. Government Securities	-	-	2,404	2,404
	\$ -	\$ -	\$ 15,179,743	15,179,743

Investments not subject to categorization:

Money market accounts	206,316
	\$ 15,386,059

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

4. RECEIVABLES

Receivables as of year end for the City's individual major funds and the non-major, and fiduciary funds in the aggregate, including the applicable allowances for uncollectible accounts, are as follows:

	Taxes	Accounts	Due from other governments	Notes	Less: Allowance for Uncollectables	Total	Due in more than one year
Governmental Activities:							
General Fund	\$ 853,451	\$ 773,391	\$ 264,834	\$ 90,927	\$ (1,183,451)	\$ 799,152	\$ 110,927
Enterprise Zone	556,812	-	-	404,690	(556,812)	404,690	368,690
Federal Grants	-	1,321	69,816	-	-	71,137	-
Nonmajor funds	354,384	-	136,597	-	(354,384)	136,597	-
Total governmental activities	\$ 1,764,647	\$ 774,712	\$ 471,247	\$ 495,617	\$ (2,094,647)	\$ 1,411,576	\$ 479,617
Business-type Activities:							
Utility services	\$ -	\$ 1,904,201	\$ 544,612	\$ -	\$ (1,270,762)	\$ 1,178,051	\$ -
Cemetery	-	1,751	-	-	-	1,751	-
Total business-type activities	\$ -	\$ 1,905,952	\$ 544,612	\$ -	\$ (1,270,762)	\$ 1,179,802	\$ -
Fiduciary Funds	\$ -	\$ 33,017	\$ 371,255	\$ -	\$ -	\$ 404,272	\$ -

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

5. CAPITAL ASSETS

Capital asset activity of the City's governmental and business-type activities was as follows:

	Beginning Balance	Additions	Disposals	Ending Balance
Governmental Activities				
Capital assets, not being depreciated:				
Land	\$ 935,896	\$ 493,945	\$ -	\$ 1,429,841
Airport land	1,932,908	-	-	1,932,908
Total capital assets not being depreciated	2,868,804	493,945	-	3,362,749
Capital assets, being depreciated:				
Roads and sidewalks	1,805,573	128,274	-	1,933,847
Airport depreciable property	9,112,065	-	-	9,112,065
Land improvements	332,920	49,394	-	382,314
Buildings and improvements	6,333,219	88,504	-	6,421,723
Vehicles	1,755,240	8,500	-	1,763,740
Computer equipment	456,437	-	-	456,437
Office equipment	208,386	136,399	(45,007)	299,778
Office furnishings	194,269	-	-	194,269
Other tools and equipment	1,622,126	90,453	-	1,712,579
Total capital assets being depreciated	21,820,235	501,524	(45,007)	22,276,752
Less accumulated depreciation for:				
Roads and sidewalks	(60,186)	(120,372)	-	(180,558)
Airport depreciable property	(6,129,036)	(149,580)	-	(6,278,616)
Land improvements	(319,119)	(1,976)	-	(321,095)
Buildings and improvements	(1,822,038)	(243,547)	-	(2,065,585)
Vehicles	(1,466,725)	(169,845)	-	(1,636,570)
Computer equipment	(426,877)	(10,982)	-	(437,859)
Office equipment	(199,081)	(10,578)	45,007	(164,652)
Office furnishings	(180,447)	(2,614)	-	(183,061)
Other tools and equipment	(1,294,942)	(91,754)	-	(1,386,696)
Total accumulated depreciation	(11,898,451)	(801,248)	45,007	(12,654,692)
Total capital assets being depreciated, net	9,921,784	(299,724)	-	9,622,060
Capital assets, net	\$ 12,790,588	\$ 194,221	\$ -	\$ 12,984,809

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

	Beginning Balance	Additions	Disposals	Ending Balance
Business-Type Activities				
Capital assets, not being depreciated:				
Land	\$ 6,736	\$ -	\$ -	\$ 6,736
Total capital assets not being depreciated	6,736	-	-	6,736
Capital assets, being depreciated:				
Water and sewer distribution systems	8,002,700	17,012	-	8,019,712
Land improvements	68,285	-	-	68,285
Buildings and building improvements	2,321,114	9,881	-	2,330,995
Vehicles	318,918	-	-	318,918
Other tools and equipment	2,163,081	23,948	-	2,187,029
Total capital assets being depreciated	12,874,098	50,841	-	12,924,939
Less accumulated depreciation for:				
Water and sewer distribution systems	(5,893,892)	(164,132)	-	(6,058,024)
Land improvements	(66,388)	(332)	-	(66,720)
Buildings and building improvements	(1,377,355)	(12,619)	-	(1,389,974)
Vehicles	(282,783)	(17,256)	-	(300,039)
Other tools and equipment	(1,745,252)	(116,579)	-	(1,861,831)
Total accumulated depreciation	(9,365,670)	(310,918)	-	(9,676,588)
Total capital assets being depreciated, net	3,508,428	(260,077)	-	3,248,351
Capital assets, net	\$ 3,515,164	\$ (260,077)	\$ -	\$ 3,255,087

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Depreciation expense was charged to programs of the primary government as follows:

Governmental Activities:

Legislative	\$ 301
General government	401,714
Public safety	166,365
Public works	82,240
Recreation and cultural	68,763
Community and economic development	81,865

Total governmental activities	<u>\$ 801,248</u>
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Business-type Activities:

Utility services	\$ 283,579
Cemetery	27,339

Total business-type activities	<u>\$ 310,918</u>
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6. INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS

The composition of interfund balances is as follows:

	Due from						Total
	General Fund	Enterprise Zone	Federal Grants	Nonmajor Governmental	Utility Services	Cemetery	
Due to							
General Fund	\$ -	\$ 2,288	\$ 290,031	\$ 45,757	\$ 695,664	\$ -	\$ 1,033,740
Enterprise Zone Fund	1,066,835	-	-	-	-	-	1,066,835
Nonmajor governmental funds	745,983	-	2,879	-	114,664	-	863,526
Utility Services Fund	34,365	107,000	-	30,000	-	34,758	206,123
Cemetery Fund	2,399	-	-	-	-	-	2,399
	<u>\$ 1,849,582</u>	<u>\$ 109,288</u>	<u>\$ 292,910</u>	<u>\$ 75,757</u>	<u>\$ 810,328</u>	<u>\$ 34,758</u>	<u>\$ 3,172,623</u>

	Advance to			
	General Fund	Enterprise Zone	Nonmajor Governmental	Total
Advance from				
General Fund	\$ -	\$ 764,116	\$ 320,146	\$ 1,084,262
Federal Grants Fund	-	-	49,825	49,825
Nonmajor governmental funds	426,867	-	172,420	599,287
Cemetery Fund	154,522	-	-	154,522
	<u>\$ 581,389</u>	<u>\$ 764,116</u>	<u>\$ 542,391</u>	<u>\$ 1,887,896</u>

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Interfund receivables are the result of timing differences in the transfer of funds to cover expenditures from shared bank accounts and grants funds where draws were received subsequent to year when expenditures occurred.

Interfund Transfers

<u>Fund Providing Resources</u>	<u>Fund Receiving Resources</u>	<u>Amount</u>
Major Street Fund	Local Street Fund	\$ 219,736
Utility Services Fund	General Fund	<u>33,036</u>
Total Transfers		<u><u>\$ 252,772</u></u>

Interfund transfers are the result of payment for services, use of City facilities by the other funds of the City, or to transfer resources from the fund that is required to receive them to the fund that is required or allowed to spend them.

7. LONG-TERM DEBT

The City issues bonds to provide for the acquisition and construction of major capital facilities. General obligation bonds are direct obligations and pledge the full faith and credit of the City. County contractual agreements and installment purchase agreements are also general obligations of the government.

Long-term obligation activity can be summarized as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Governmental Activities					
Emergency loans payable	\$ 132,000	\$ -	\$ 98,000	\$ 34,000	\$ 34,000
ULA loan payable	67,286	-	-	67,286	67,286
Core Communities loan payable	200,000	-	-	200,000	-
HUD Section 108 loan	450,000	-	-	450,000	100,000
Dump trucks lease	111,581	-	20,552	91,029	22,020
Photocopiers lease	-	126,086	7,220	118,866	29,724
Subtotal - installment debt	960,867	126,086	125,772	961,181	253,030
Compensated absences	246,221	268,315	218,582	295,954	142,534
Total governmental activities	<u><u>\$ 1,207,088</u></u>	<u><u>\$ 394,401</u></u>	<u><u>\$ 344,354</u></u>	<u><u>\$ 1,257,135</u></u>	<u><u>\$ 395,564</u></u>

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

For governmental activities, compensated absences are typically liquidated by the General Fund.

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Business-type Activities					
1997 Water bonds	\$ 845,000	\$ -	\$ 160,000	\$ 685,000	\$ 170,000
Cemetery equipment	41,687	-	10,815	30,872	11,048
Photocopier lease	-	3,244	56	3,188	768
Subtotal - installment debt	886,687	3,244	170,871	719,060	181,816
Deferred amount on refunding	(33,146)	-	(6,858)	(26,288)	(6,858)
Compensated absences	66,588	33,163	45,092	54,659	21,417
Total business-type activities	\$ 920,129	\$ 36,407	\$ 209,105	\$ 747,431	\$ 196,375

Annual debt service requirements to maturity for the above obligations are as follows:

	Governmental Activities		
	Principal	Interest	Total
2005	\$ 253,030	\$ 16,354	\$ 269,384
2006	254,714	9,896	264,610
2007	157,862	5,249	163,111
2008	95,575	1,196	96,771
2009	2,079	3,000	5,079
2010 - 2014	50,867	55,786	106,653
2015 - 2019	63,631	32,864	96,495
2020 - 2024	83,423	13,072	96,495
	\$ 961,181	\$ 137,417	\$ 1,098,598
	Business-type Activities		
	Principal	Interest	Total
2005	\$ 181,816	\$ 31,598	\$ 213,414
2006	192,555	23,548	216,103
2007	193,981	14,922	208,903
2008	150,708	6,583	157,291
	\$ 719,060	\$ 76,651	\$ 795,711

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

8. RISK MANAGEMENT

The City is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The City has purchased commercial insurance for all of these various risks. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

9. PENSION PLAN – GENERAL EMPLOYEES' RETIREMENT SYSTEM

Plan Description

The General Employees' Pension Plan is a single-employer defined benefit pension plan that is administered by the City of Benton Harbor General Employees' Retirement System. This Plan covers all appointed officers and employees of the City (except personnel of the Fire and Police departments) and appointed officers and employees of the Southwest Michigan Regional Airport Authority. The system provides retirement, disability and death benefits to Plan members and their beneficiaries. At July 1, 2003, the date of the most recent actuarial valuation, membership consisted of 48 retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits but not yet receiving them, and 79 current active employees. The plan does not issue a separate financial report.

Summary of Significant Accounting Policies

The financial statements of the Plan are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. The City's contributions are recognized when due and a formal commitment to provide the contributions has been made. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. All plan investments are reported at fair value.

Funding Policy

The obligation to contribute to and maintain the system for these employees was established by negotiation with the City's collective bargaining units and requires a contribution from the employees of 3 percent. The funding policy provides for periodic employer contributions at actuarially determined rates. Administrative costs of the Plan are financed through investment earnings.

Annual Pension Costs

For the year ended June 30, 2004, the City's annual pension cost of \$93,006 for the Plan was equal to the required and actual contribution. The annual required contribution was determined as part of an actuarial valuation at July 1, 2003, using the aggregate actuarial cost method. Significant actuarial assumptions used include: (a) a 7.75 percent investment rate of return; (b) projected salary increases of 4 percent per year; and (c) no cost of living adjustments. Both (a) and (b) include an inflation component. The actuarial value of assets was determined using fair market values. The unfunded actuarial liability is being amortized as a level percentage of payroll on a closed basis, over 30 years.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Three-year trend information as of June 30 follows:

	<u>Fiscal Year Ended June 30</u>		
	<u>2002</u>	<u>2003</u>	<u>2004</u>
Annual pension costs (APC)	\$ 6,422	\$ 201,109	\$ 93,006
Percentage of APC contributed	100%	100%	100%
Net pension obligation	\$ -	\$ -	\$ -

10. PENSION PLAN - POLICE AND FIRE RETIREMENT SYSTEM PLAN DESCRIPTION

Plan Description

The Police and Fire Pension Plan is a single-employer defined benefit pension plan that is administered by the City of Benton Harbor Police and Fire Employees Retirement system/this Plan covers all full-time police and fire employees of the City. The system provides retirement, disability and death benefits to Plan members and their beneficiaries. At July 1, 2003, the date of the most recent actuarial valuation, membership consisted of 59 retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits but not yet receiving them, and 37 current active employees. The Plan does not issue a separate financial report.

Summary of Significant Accounting Policies

The financial statements of the Plan are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. The City's contributions are recognized when due and a formal commitment to provide the contributions has been made. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. All plan investments are reported at fair value.

Funding Policy

The obligation to contribute to and maintain the system for these employees was established by negotiation with the City's collective bargaining units, and requires a contribution from the employees of 5 percent for police employees and 6 percent for fire employees. The funding policy provides for periodic employer contributions at actuarially determined rates. Administrative costs of the Plan are financed through investment earnings.

Annual Pension Cost

For the year ended June 30, 2004, the City's annual pension cost of \$318,048 for the Plan was equal to the City's actual and required contribution. Of this amount, \$229,451 was funded by the tax levy described below and recorded as "property taxes" on the Statement of Changes in Plan Net Assets. The annual required contribution was determined as part of an actuarial valuation at July 1, 2003, using the aggregate actuarial cost method. Significant actuarial assumptions used include (a) a 7.75 percent investment rate of return, (b) projected salary increases of 4 percent per year, and (c) 4 percent per year cost of living adjustments. Both (a) and (b) include an inflation component. The unfunded actuarial liability is being amortized as a level percentage of payroll on a closed basis. The remaining amortization period is 27 to 30 years.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

On August 14, 1984, the Circuit Court for Berrien County ordered the City of Benton Harbor to pay off the then calculated \$2,597,299 unfunded liability over the next 30 years. The City must levy a sufficient additional millage on an annual basis to pay the portion of this 30 year amortization plus normal operating costs that are not covered under the general operating budget. As indicated above, during the year \$229,451 was recorded as property tax revenue. Due to the age of this commitment, the actuary has not included this as a net pension obligation.

Three-year trend information as of June 30 follows:

	<u>Fiscal Year Ended June 30</u>		
	<u>2002</u>	<u>2003</u>	<u>2004</u>
Annual pension costs (APC)	\$ 362,562	\$ 370,738	\$ 318,048
Percentage of APC contributed	100%	100%	100%
Net pension obligation	\$ -	\$ -	\$ -

11. CONTINGENCIES

The City is arbitrating several illegal discharge cases. In all of these cases, retroactive pay or pay adjustments may be required. Currently, the City is unable to presently predict the outcome of the range of potential loss, if any, which may result from the disposition of these matters.

The City is also the defendant in various litigations involving wrongful death, challenges to various City ordinances, various real estate disputes, breach of contract and violation of civil rights. The civil suits will likely be covered by the City's liability insurance.

City management considers the City's exposure under all of the suits to be immaterial. No provision for any loss has been made in the financial statements.

12. CONSTRUCTION CODE FEES

The City oversees building construction, in accordance with the State's construction code act, including inspection of building codes. The city charges fees for these services. Beginning in January 1, 2000, the law requires that collection of these fees be used only for construction code costs, including an allocation of estimated overhead costs. A summary of the current year activity and the cumulative shortfall generated since January 1, 2000, is as follows:

Deficit - July 1, 2003	\$ (248,106)
Building permit revenue	128,076
Construction code expenses	<u>(183,902)</u>
Accumulated shortfall - June 30, 2004	<u>\$ (303,932)</u>

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

13. RESTATEMENT

Beginning net assets of the general fund were increased by \$11,036 to reflect the consolidation of the Economic Development Corporation special revenue fund into the general fund beginning with the current year.

* * * * *

REQUIRED SUPPLEMENTARY INFORMATION

City of Benton Harbor, Michigan
Required Supplementary Information

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (A)	Actuarial Accrued Liability (B)	Unfunded AAL (UAAL) (A-B)	Funded Ratio (A/B)	Covered Payroll (C)	UAAL as a % of Covered Payroll
<u>General Employees' Retirement System</u>						
06/30/1996	\$ 4,454,536	\$ 3,320,264	\$ 1,134,272	134.2%	\$ 1,762,685	-n/a-
06/30/1998	5,812,916	3,677,567	2,135,349	158.1%	2,235,027	-n/a-
06/30/2000	6,674,675	5,245,864	1,428,811	127.2%	2,506,666	-n/a-
06/30/2001	6,167,942	5,541,517	626,425	111.3%	2,533,613	-n/a-
06/30/2002	6,253,841	6,173,546	80,295	101.3%	2,610,223	-n/a-
06/30/2003	6,436,460	6,276,034	160,426	102.6%	2,592,799	-n/a-

Police and Fire Retirement System

06/30/1996	7,538,334	7,761,331	(222,997)	97.1%	1,401,406	15.9%
06/30/1998	10,089,128	9,030,330	1,058,798	111.7%	1,515,908	-n/a-
06/30/2000	10,856,074	10,811,520	44,554	100.4%	1,346,128	-n/a-
06/30/2001	10,004,228	11,672,480	(1,668,252)	85.7%	1,351,244	123.5%
06/30/2002	10,210,869	12,109,175	(1,898,306)	84.3%	1,231,468	154.1%
06/30/2003	10,235,411	11,884,761	(1,649,350)	86.1%	1,349,989	122.2%

Schedule of Employer Contributions

<u>Year Ended June 30</u>	<u>Annual Required Contributions</u>	<u>Percentage Contributed</u>
<u>General Employees' Retirement System</u>		
1999	\$ 184,169	100%
2000	256,298	100%
2001	6,686	100%
2002	6,422	100%
2003	201,109	100%
2004	93,006	100%
<u>Police and Fire Retirement System</u>		
1999	\$ 296,377	100%
2000	254,773	100%
2001	156,970	100%
2002	362,562	100%
2003	370,738	100%
2004	318,048	100%

COMBINING AND INDIVIDUAL FUND FINANCIAL
STATEMENTS and SCHEDULES

City of Benton Harbor, Michigan
Combining Balance Sheet
Nonmajor Governmental Funds
June 30, 2004

	Special Revenue		
	Major Streets	Local Streets	State Grants
Assets			
Cash and cash equivalents	\$ 72,286	\$ -	\$ -
Due from other governments	102,008	34,589	-
Due from other funds	114,664	-	2,879
Advances to other funds	222,245	-	-
<u>TOTAL ASSETS</u>	\$ 511,203	\$ 34,589	\$ 2,879
<u>LIABILITIES AND FUND BALANCES</u>			
Liabilities			
Accounts payable	\$ 5,000	\$ 8,102	\$ (306)
Accrued liabilities	4,189	7,645	-
Due to other funds	45,757	-	-
Advances from other funds	307,836	222,245	69,206
Total liabilities	362,782	237,992	68,900
Fund balances (deficit)			
Reserved for advances	222,245	-	-
Unreserved, undesignated (deficit)	(73,824)	(203,403)	(66,021)
Total fund balances (deficit)	148,421	(203,403)	(66,021)
<u>TOTAL LIABILITIES, AND FUND BALANCES</u>	\$ 511,203	\$ 34,589	\$ 2,879

Debt Service	Permanent Public Improvement	Totals
\$ 35,461	\$ (874)	\$ 106,873
-	-	136,597
636,073	109,910	863,526
-	320,146	542,391

\$ 671,534	\$ 429,182	\$ 1,649,387
------------	------------	--------------

\$ -	\$ 1,390	\$ 14,186
-	-	11,834
30,000	-	75,757
-	-	599,287

30,000	1,390	701,064
--------	-------	---------

-	320,146	542,391
641,534	107,646	405,932

641,534	427,792	948,323
---------	---------	---------

\$ 671,534	\$ 429,182	\$ 1,649,387
------------	------------	--------------

City of Benton Harbor, Michigan
Combining Statement of Revenue, Expenditures and Changes in Fund Balances
Nonmajor Governmental Funds
For the Year Ended June 30, 2004

	Special Revenue		
	Major Streets	Local Streets	State Grants
Revenue			
Taxes	\$ -	\$ -	\$ -
State sources	698,399	219,251	-
Interest	472	-	-
Total revenue	699,731	219,251	-
Expenditures			
Current:			
Public works:			
Road maintenance	387,093	429,590	-
Administation	41,591	28,836	-
Community and economic development	-	-	(306)
Debt service:			
Principal	-	-	-
Interest	-	-	-
Total expenditures	428,684	458,426	(306)
Revenue (under) expenditures	271,047	(239,175)	306
Other financing sources (uses)			
Transfers in	-	219,736	-
Transfers (out)	(219,736)	-	-
Total other financing sources	(219,736)	219,736	-
Net changes in fund balances	51,311	(19,439)	306
Fund balances (deficit), beginning of year	97,110	(183,964)	(66,327)
Fund balances (deficit), end of year	\$ 148,421	\$ (203,403)	\$ (66,021)

Debt Service	Permanent Public Improvement	Totals
\$ 386,913	\$ 138,494	\$ 525,407
-	-	917,650
10	4	486
386,923	138,498	1,444,403
-	-	816,683
-	-	70,427
-	24,274	23,968
98,000	-	98,000
3,625	-	3,625
101,625	24,274	1,012,703
285,298	114,224	431,700
-	-	219,736
-	-	(219,736)
-	-	-
285,298	114,224	431,700
356,236	313,568	516,623
\$ 641,534	\$ 427,792	\$ 948,323

City of Benton Harbor, Michigan
Combining Statement of Fiduciary Net Assets
Pension Trust Funds
June 30, 2004

	General Employees' Retirement System	Police and Fire Retirement System	Totals
Assets			
Cash and cash equivalents	\$ 17,519	\$ 128,491	\$ 146,010
Investments:			
Corporate bonds	2,258,769	3,728,916	5,987,685
Corporate stocks	3,478,673	5,710,981	9,189,654
US Government securities	1,202	1,202	2,404
Money market	139,643	66,673	206,316
Receivables:			
Accrued interest	12,470	20,547	33,017
Other	236,114	135,141	371,255
Total assets	6,144,390	9,791,951	15,936,341
Liabilities			
Due to resigned employees	18,828	6,399	25,227
Accrued and other liabilities	-	189,956	189,956
Total liabilities	18,828	196,355	215,183
Net Assets			
Held in trust for pension			
benefits and other purposes	\$ 6,125,562	\$ 9,595,596	\$ 15,721,158

City of Benton Harbor, Michigan
Combining Statement of Changes in Fiduciary Net Assets
Pension Trust Funds
For the Year Ended June 30, 2004

	General Employees' Retirement System	Police and Fire Retirement System	Totals
Additions			
Taxes	\$ -	\$ 229,451	\$ 229,451
Contributions:			
Employer	93,006	88,597	181,603
Employee	88,556	101,273	189,829
Total contributions	181,562	189,870	371,432
Investment earnings:			
Net appreciation in fair value of investments	428,038	693,092	1,121,130
Interest and dividends	176,797	296,905	473,702
Net investment earnings	604,835	989,997	1,594,832
Total additions	786,397	1,409,318	2,195,715
Deductions			
Pension benefits paid directly to participants	302,207	855,448	1,157,655
Administrative expenses	77,711	78,613	156,324
Total deductions	379,918	934,061	1,313,979
Change in net assets	406,479	475,257	881,736
Net assets, beginning of year	5,719,083	9,120,339	14,839,422
Net assets, end of year	\$ 6,125,562	\$ 9,595,596	\$ 15,721,158

City of Benton Harbor, Michigan



Berrien County

SINGLE AUDIT

For the Year Ended June 30, 2004



REHMANN ROBSON

Certified Public Accountants

**CITY OF BENTON HARBOR, MICHIGAN
SINGLE AUDIT**

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REHMANN ROBSON

Certified Public Accountants

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**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE
AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

December 17, 2004

Honorable Mayor and Members
of the City Commission
City of Benton Harbor, Michigan

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the ***City of Benton Harbor, Michigan*** as of and for the year ended June 30, 2004, which collectively comprise the City's basic financial statements, and have issued our report thereon dated December 17, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the City of Benton Harbor, Michigan's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

However, we noted other matters involving compliance that we have reported to the management of the City of Benton Harbor, Michigan in a separate letter dated December 17, 2004.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City of Benton Harbor, Michigan's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our report noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

However, we noted other matters involving the internal control over financial reporting that we have reported to the management of the City of Benton Harbor, Michigan in a separate letter dated December 17, 2004.

This report is intended solely for the information and use of the audit committee, management, others within the organization, the City Commission, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style.



REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP

 an independent member of
BAKER TILLY
INTERNATIONAL

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH
REQUIREMENTS APPLICABLE TO MAJOR PROGRAMS
AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE
WITH OMB CIRCULAR A-133**

December 17, 2004

Honorable Mayor and Members
of the City Commission
City of Benton Harbor, Michigan

Compliance

We have audited the compliance of the *City of Benton Harbor, Michigan* with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal programs for the year ended June 30, 2004. The City of Benton Harbor, Michigan's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal programs are the responsibility of the City of Benton Harbor, Michigan's management. Our responsibility is to express an opinion on the City of Benton Harbor, Michigan's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on major federal programs occurred. An audit includes examining, on a test basis, evidence about the City of Benton Harbor, Michigan's compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City of Benton Harbor, Michigan's compliance with those requirements.

As described in item 2004-1 in the accompanying schedule of findings and questioned costs, the City of Benton Harbor, Michigan did not comply with requirements regarding the Davis-Bacon Act that are applicable to its Community Development Block Grant program. Compliance with such requirements is necessary, in our opinion, for the City of Benton Harbor, Michigan to comply with requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the City complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended June 30, 2004.

We also noted other matters involving compliance that we have reported to the management of the City of Benton Harbor, Michigan in a separate letter dated December 17, 2004.

Internal Control Over Compliance

The management of the City of Benton Harbor, Michigan is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the City of Benton Harbor, Michigan's internal control over compliance with requirements that could have a direct and material effect on major federal programs in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted a matter involving the internal control over compliance and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the City's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants. The reportable condition is described in the accompanying schedule of findings and questioned costs as item 2004-1.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. We consider the reportable condition described above to be material weaknesses.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the ***City of Benton Harbor, Michigan*** as of and for the year ended June 30, 2004, which collectively comprise the City's basic financial statements, and have issued our report thereon dated December 17, 2004. Our audit was performed for the purpose of forming opinions on the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

This report is intended solely for the information and use of the audit committee, management, others within the organization, the City Commission, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



City of Benton Harbor
Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2004

Federal/Pass-through Grantor Program Title	CFDA Number	Federal/ Pass-through Grantor Number	Federal Expenditures
U.S. Department of Housing and Urban Development			
Direct Programs:			
Community Development Block Grant			
Program year 2001-2002	14.218	B-01-MC-26-0035	\$ 1,475
Program year 2002-2003	14.218	B-02-MC-26-0035	590,739
 Brownfield Economic Development Grant	 14.248	 B-98-MC-26-0035	 <u>493,945</u>
 Total U.S. Department of Housing and Urban Development			 1,086,159
U.S. Department of Justice			
Direct Program:			
Local Law Enforcement Block Grant			
Program year 2003-2004	16.592	2003-LB-BX-1739	<u>47,634</u>
 Total Expenditures of Federal Awards			 <u><u>\$ 1,133,793</u></u>

CITY OF BENTON HARBOR, MICHIGAN

Notes to Schedule of Expenditures of Federal Awards

1. BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards presents the activity of all federal awards programs of the City of Benton Harbor, Michigan (the "City"). Federal awards received directly from federal agencies, as well as federal awards passed through other government agencies, are included on the schedule.

The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

The City of Benton Harbor reporting entity is defined in Note 1 of the City's financial statements.

2. SUBRECIPIENTS

The City of Benton Harbor did not provide federal awards to subrecipients during the current year.

3. EXPENDITURES MADE ON BEHALF OF THE CITY OF BENTON HARBOR

During the year ended June 30, 2004, the State of Michigan Department of Transportation expended \$267,369 on various street projects in the City of Benton Harbor. These expenditures were federally funded under CFDA number 20.205, and were incurred directly by the State of Michigan. No funds were passed-through the City of Benton Harbor for these projects. Accordingly, these expenditures are excluded from the City's Schedule of Expenditures of Federal Awards.

* * * * *

CITY OF BENTON HARBOR, MICHIGAN

Schedule of Findings and Questioned Costs

For the Year Ended June 30, 2004

SECTION I - SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued:

Unqualified

Internal control over financial reporting:

Material weakness(es) identified?

_____ yes X no

Reportable condition(s) identified
not considered to be material weaknesses?

_____ yes X none reported

Noncompliance material to financial statements
noted?

_____ yes X no

Federal Awards

Internal Control over major programs:

Material weakness(es) identified?

X yes _____ no

Reportable condition(s) identified
not considered to be material weaknesses?

_____ yes X none reported

Type of auditors' report issued on compliance
for major programs:

Qualified

Any audit findings disclosed that are required
to be reported in accordance with
Circular A-133, Section 510(a)?

X yes _____ no

CITY OF BENTON HARBOR, MICHIGAN

Schedule of Findings and Questioned Costs (Continued)

For the Year Ended June 30, 2004

SECTION I - SUMMARY OF AUDITORS' RESULTS (Concluded)

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
14.218	Community Development Block Grant
14.248	Brownfield Economic Development Grant

Dollar threshold used to distinguish
between Type A and Type B programs: \$300,000

Auditee qualified as low-risk auditee? yes X no

SECTION II – FINANCIAL STATEMENT FINDINGS

None.

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

2004-1 HUD - CDBG Davis-Bacon Compliance

In the report on the City's 2003 single audit, it was noted that the City was not retaining sufficient documentation to demonstrate it was complying with the prevailing wage requirements of the Davis-Bacon Act.

While the City took corrective action to resolve this issue and began retaining the required information subsequent to June 30, 2004, this condition remained unchanged throughout the period under audit. Accordingly, since the City was unable to provide documentation of its efforts to comply with the Davis-Bacon requirements applicable to its CDBG program for the year ended June 30, 2004, this finding has been repeated.

No costs were questioned as a result of this finding.

CITY OF BENTON HARBOR, MICHIGAN

Schedule of Findings and Questioned Costs (Concluded)

For the Year Ended June 30, 2004

SECTION IV – PRIOR YEAR FINDINGS

Financial Statement Findings

None.

Federal Award Findings

2003-1 HUD - CDBG Financial Reports not Reconciled Against the General Ledger

During the current year, there were no material differences between the amounts reported as expended to the Department of Housing and Urban Development and the amounts reported on the City's general ledger. Accordingly, this finding is considered to be resolved.

2003-2 HUD - CDBG Davis-Bacon Compliance

This finding remained unresolved at June 30, 2004, and has been repeated as finding 2004-1.

* * * * *



REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP



December 17, 2004

The Honorable Mayor and
Members of the City Commission
The City of Benton Harbor
Benton Harbor, Michigan

We have audited the financial statements of the City of Benton Harbor for the year ended June 30, 2004, and have issued our report thereon dated December 17, 2004. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under Auditing Standards Generally Accepted in the United States of America and OMB Circular A-133

As stated in our engagement letter dated September 1, 2004, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

In planning and performing our audit, we considered the City of Benton Harbor's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. We also considered internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

As part of obtaining reasonable assurance about whether the City of Benton Harbor's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit. Also, in accordance with OMB Circular A-133, we examined, on a test basis, evidence about the City of Benton Harbor's compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* applicable to each of its major federal programs for the purpose of expressing an opinion on the City of Benton Harbor's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the City of Benton Harbor's compliance with those requirements.

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we advised management about the appropriateness of accounting policies and their application. The significant accounting policies used by the City of Benton Harbor are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by the City of Benton Harbor during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

- Management's estimate of the useful lives of other depreciable fixed assets is based on the length of time it is believed that those assets will provide some economic benefit in the future. We evaluated the key factors and assumptions used to develop the useful lives of those assets in determining that they are reasonable in relation to the financial statements taken as a whole.
- Management's estimate of the various allowances made for uncollectable accounts receivable is based on past collection history. We evaluated the key factors and assumptions used to develop the allowances in determining that they are reasonable in relation to the financial statements taken as a whole.

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the City's financial reporting process (that is, cause future financial statements to be materially misstated). The City has posted all journal entries that we have identified as significant, and their effect is included in the City's financial statements.

In addition, the attached schedule summarizes uncorrected misstatements of the financial statements. Management has determined that their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. Throughout the year, the City engaged the services of another CPA firm to assist with various accounting duties and the preparation for the annual audit. During the course of our audit, we coordinated many of our inquiries and tests with both City management and the City's contracted accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City of Benton Harbor's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing our audit.

This letter and the accompanying memorandum are intended for the use of the City Commission, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

A handwritten signature in black ink, appearing to read "Lehmann Lohman". The signature is written in a cursive, flowing style.

City of Benton Harbor
Comments and Recommendations
For the Year Ended June 30, 2004

During our audit we became aware of certain issues regarding internal control and financial reporting. This memorandum summarizes our comments and suggestions regarding these matters. This memorandum does not affect our report dated December 17, 2004 on the financial statements of the City of Benton Harbor.

Overall Financial Condition

As management is keenly aware, the City has been experiencing some extremely tough economic times. Despite having placed a deficit elimination plan in effect (as disclosed in Note 2 to the financial statements), during the year ended June 30, 2004, the City's accumulated unreserved fund deficit in the general fund grew by almost one million dollars to \$2.2 million. In addition, the City reported fund deficits totaling \$643,491 in five other funds. On a full accrual perspective, the City's combined governmental activities reported an unrestricted deficit in net assets of \$2.1 million.

This condition contributed to the City's inability to make certain required payments to other units of government in a timely manner throughout the year, and continues to raise concerns about the City's financial solvency and its ongoing ability to provide and finance key governmental services.

Obviously, there is no easy solution for the City's current financial condition. Nevertheless, we recommend that the City continue to make rebuilding its fiscal solvency one of its most paramount objectives over the next few years.

Periodic Account Analyses

As noted in the prior year, the City has not been performing monthly account analyses or reconciliations for many of its balance sheet accounts. Our review of the general ledger revealed that a significant effort was again undertaken at year end to substantially adjust the City's accounting records to present information in accordance with generally accepted accounting principles.

While we were ultimately satisfied that the amounts presented in the City's audited financial statements were fairly presented in all material respects, the significant amount of corrections required at year end underscores that the interim financial data available to City management is not materially accurate or reliable.

One of the best internal control procedures for verifying the accuracy of the City's financial information through the year is the periodic analysis of account balances (particularly for balance sheet accounts) to ascertain the following:

- Balance sheet accounts are supported by itemized listings of the components comprising the financial statement totals;
- The detail listing is free of obvious errors, unusual reconciling items that suggest the need for adjustment, and mispostings or other clerical errors;
- The balances make sense relative to operational data

City of Benton Harbor

Comments and Recommendations

For the Year Ended June 30, 2004

Accordingly, we repeat our recommendation that all balance sheet accounts be analyzed monthly. The analyses should be retained and reviewed by a responsible official other than the preparer as part of the monthly closing cycle. This procedure will provide improved assurance that accounting errors will be detected and corrected in a timely manner, and will provide management and the City Commission more meaningful and useful financial data with which to make their decisions.

Approval for Disbursements

During our testing of internal controls over cash disbursements, we noted that in nearly 25% of the invoices selected for testing required signatures were missing from check requests authorizing disbursements. This condition was also noted in the prior year's audit. We recommend that the City carefully adhere to its stated policy of requiring written authorization from appropriate officials for all disbursements.

* * * * *

City of Benton Harbor
Schedule of Adjustments Passed (SOAP)
For the June 30, 2003 Audit

In accordance with the provisions of SAS 89, *Audit Adjustments*, we have prepared the following schedule of proposed audit adjustments, which we believe are immaterial both individually and in the aggregate. Also in accordance with SAS 89, we are providing this schedule to both management and the audit committee to receive their assurance that they agree that the amounts listed below are not material to the financial statements, either individually or in the aggregate, and do not need to be recorded.

Effect of Passed Adjustment - Over(Under)Statement						
	Assets	Liabilities	Beginning Equity	Revenue	Expenses/ Expenditures	W/P Ref
Special Revenue Fund - Enterprise Zone						
July 2004 expense was improperly included in accounts payable	-	17,338	-	-	17,338	ALF AA-2//3
Cemetery Enterprise Fund						
Certificates of deposit carried at cost, rather than market	(4,229)	-	-	(4,229)	-	ALF A-2/1